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In the Supreme Court of the United States

October Term 1955

EDWARD S. CANTON,

Petitioner,

vs.

UNITED STATES OF AMERICA.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

Edward S. Canton prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Eighth Circuit entered in this cause on October 20, 1955.

OPINIONS BELOW

The order of the District Court denying petitioner's motion, following a verdict of guilty, for a judgment of acquittal or, in the alternative, for a new trial is not reported but is printed in the record. (R. 207-213.) The opinion of the Court of Appeals is reported in 226 F. 2d — and is printed as an appendix to this petition.[1]

[1] Page references to the opinion are to the pages in the appendix.

JURISDICTION

The judgment of the Court of Appeals was entered October 20, 1955. As permitted by Rule 15 of that court, a petition for rehearing was filed on November 7, 1955. An order denying the same was entered November 15, 1955. The jurisdiction of this Court is invoked under Title 28 U. S. C. §1254 (c. 646, 62 Stat. 928) and Title 18 U. S. C. §3772 (c. 645, 62 Stat. 846), as prescribed by Rule 37 (b) of the Federal Rules of Criminal Procedure.

QUESTIONS PRESENTED

1. Whether in a prosecution for violation of 26 U. S. C. §145 (b) by the filing of a fraudulent income-tax return, it is proper to permit the Government to resort to a circumstantial method (cash receipts and disbursements) of proving understatement and wilfulness when it appears and the Government concedes that there is no independent evidence of a likely source of unreported income not susceptible of direct proof on the basis of available books and records.

2. Whether in such a prosecution it is proper to permit the Government to prove understatement and willfulness according to the cash method of accounting when the accrual method of accounting was employed in keeping the defendant's books (and the court so instructed the jury without objection by the Government) and it is possible to prove income according to the latter method from available books and records.

3. Whether a document is a "return" for purposes of prosecution under §145 (b) which, though it bears the name of the defendant, was not signed by him but by an-

other, and there is no showing that the defendant authorized such other person to inscribe his name or that he ever saw the document or was informed of its contents.

STATUTES INVOLVED

Internal Revenue Code of 1939 (26 U. S. C., c. 2, 53 Stat. 1-503):

Section 145. Penalties.

(a) Failure to File Returns, Submit Information, or Pay Estimated Tax or Tax.—Any person required under this chapter * * * to make a return * * * who willfully fails to * * * make such return * * * at the time or times required by law or regulations, shall, in addition to other penalties provided by law, be guilty of a misdemeanor and, upon conviction thereof, be fined not more than $10,000, or imprisoned for not more than one year, or both, together with the costs of prosecution.

(b) Failure to Collect and Pay Over Tax, or Attempt to Defeat or Evade Tax.—Any person * * * who willfully attempts in any manner to evade or defeat any tax imposed by this chapter or the payment thereof, shall, in addition to other penalties provided by law, be guilty of a felony and, upon conviction thereof, be fined not more than $10,000, or imprisoned for not more than five years, or both, together with the costs of prosecution.

STATEMENT

The petitioner was found guilty by the verdict of a jury of violating 26 U. S. C. §145 (b) "by filing and causing to be filed" a "fraudulent income tax return" for 1947. (R. 1, 205.) He appealed from an order denying his motion for a judgment of acquittal or, in the alternative, for a new trial and from the judgment based on the verdict. (R. 205-215.) The judgment was affirmed on appeal.

The petitioner has for many years been engaged in business in Minneapolis as a wholesale lumber dealer, until 1950 as a sole proprietor under the name Canton Lumber Sales Company. (R. 16, 119-120, 127; Op. 2.) There was a shortage of lumber during and after World War II, and in the fall of 1945 he visited mills on the West Coast, his principal suppliers, in a vain effort to secure an increased supply from them. (R. 38, 127-128; Op. 2.) He then joined with one Baldridge, an experienced mill operator, in the purchase of a mill at Drain, Oregon, which was incorporated as Douglas Timber Corporation. In March, 1946, just as operations were getting under way, Baldridge, who was to be in charge of the mill, died unexpectedly, and the petitioner, who was then en route to Minneapolis, returned to Drain and, notwithstanding lack of experience in the management of sawmill and timber operations, took over Baldridge's job. Except for occasional hurried visits to Minneapolis, the petitioner remained on the West Coast until October, 1948, when the mill was sold. (R. 42, 128-129, 141, 151, 162-163, 259-260; Op. 2-3.) During this period the employees at the petitioner's Minneapolis office were not to exceed three in number—two salesmen and a bookkeeper, the latter until about March, 1948, an 18-year-old niece hired in the fall of 1945. (R. 14, 41, 127; Op. 3.)

Maintained at the petitioner's Minneapolis office and received in evidence were order files (perhaps a thousand in number) with respect to all purchases and sales of lumber during 1946 and 1947, including the originals or copies of all invoices and other documents relating to such transactions; order books recording all orders taken from retailers; a car journal containing pertinent information with respect to all purchases and sales, including the com-

puted amount of gross profit on each sale; customer ledgers showing the amount billed to each customer and the amount paid; and for each year a so-called "cash book" maintained for the purpose of recording all items of income and all items of expense. (R. 15-16, 17, 18, 19, 21, 32, 37, 63; Op. 3.). The so-called cash books were kept according to the accrual method of accounting, and the jury was so instructed without objection by the government. (R. 193-194; Op. 20.) The reported net income was computed by an outsider on the basis only of such 1947 "cash" book. (R. 141, 143, 152-154; Op. 3; Ex. 13, Supp. R. 65-147.)

The petitioner's 1947 net income was reported as $26,105.99. (R. 223-227.) Concededly omitted from reported gross income were the following items and amounts of taxable income (R. 191; Op. 4):

(a) Special 5% discount on purchases from Douglas representing commissions payable by Douglas to the petitioner on sales by Douglas to Canton Lumber Sales Company	$5,531.03
(b) Net excess of 2% discounts received for prompt payment over like discounts granted for prompt payment	488.23
(c) An interest check received from Douglas	1,001.39
(d) Two checks (one for $1,062.80 and the other for $848.21) representing commissions payable by Douglas to the petitioner on sales by Douglas to others than Canton Lumber Sales Company	1,911.01
Total	$8,931.66

(R. 65, 78, 79, 88, 96, 107, 110-111, 245; Op. 4.)

As to items (a) and (b), the correct discounts were shown by the petitioner's order files and customer ledgers, and these two understatements reflect 477 discrepancies (both for and against the petitioner) between the amounts of gross profit shown by such files and ledgers (which were in all respects accurate) and the amounts of gross profit entered by the bookkeeper in the "cash" book from which the return was prepared. (R. 63, 69, 85, 87, 105, 107.) Receipt of the three checks represented by items (c) and (d), contrary to what was true with respect to prior like checks, was not recorded in the "cash" book; however, the payment of these amounts was shown by the Douglas books and records. (R. 78, 79, 88, 244, 245.)

Aside from what is referred to as the $10,000 Paul Canton item, the Government did not assert that there was any unreported income other than the four items set out above. (R. 71-72, 85-86.) The $10,000 Paul Canton item represented a loan to the petitioner in that amount made by the petitioner's brother in January, 1947, and by him cancelled in July, 1947. Both the loan and its cancellation were recorded in the petitioner's books. (R. 237-239.) The petitioner contended that the cancellation was a gift, not income, and this question was left to the jury. (R. 189, 197-198.)

The Government sought at the outset (R. 6) to prove net income and consequent understatement by offering evidence of cash receipts and disbursements, principally bank deposits and withdrawals and "analyses" thereof. The petitioner objected on the ground, in substance (R. 6-8), that a condition precedent to resort to circumstantial methods of proof is some sort of showing that there is unre-

ported income which cannot be established by direct proof, pointing out in this connection that while concededly certain items of gross income were not reported, all such items could be proved by the petitioner's records and those of the Douglas Company; and on the further ground (R. 26) that there was no showing that the petitioner was on the cash rather than the accrual basis of accounting. The court was disposed to agree, at times on one ground and at times on the other or on both (R. 8-10, 10-11, 25-27, 30-32, 34-35, 48, 54-56, 67-68, 69), and deferred ruling "until you have laid further foundation." (R. 10, 25.) In response to a question by the court as to what the Government's theory was—whether the petitioner had transactions "not noted on the books" or "had omitted transactions"—, Government counsel replied only that "I don't know the answer except that on the bank deposit method it comes out more." (R. 69.) At another point in the same colloquy counsel answered "No" to the court's question, "Is it your position that you cannot determine his income from the books and records if he was on the cash basis?" (R. 67-68.)

Though the court appears intermittently to have deviated from its announced position, in that it received "analyses" of cancelled checks and of bank deposits (notwithstanding that the deposits themselves were not in evidence) and "summaries" of cash receipts and disbursements (R. 25-27, 27-28, 56-57, 60, 61), it continued for the most part to adhere to this position (R. 67-69) until the Government's special agent in charge of the case was called to the stand and testified (R. 70) that in his opinion the petitioner "is on the cash basis" and "his books and records do not reflect his income." (R. 69-70.)

On the basis alone of this opinion, notwithstanding that the witness, in response to the court's own questions, stated (R. 71-72) that he knew of no specific items of income that could not be proved on the basis of books and records, the court permitted the witness to be withdrawn without cross examination (though granted later (R. 85)) and received in evidence deposit records theretofore excluded (R. 74) and also, through other witnesses (R. 75-77, 82-84), other records bearing on cash receipts and disbursements, all of which culminated ultimately in Exhibit 105, which, on the basis of cash receipts and disbursements, purported to reflect a net income of $50,743.72, inclusive of the $10,000 cancelled loan, as against the $26,105.99 reported on the accrual basis (R. 102, 227, 249-250).

It was on Exhibit 105 that the Government largely based its appeal to the jury for a verdict of guilty (Supp. R. 23-26), and the exhibit in enlarged form went to the jury room (R. 102, 202). The petitioner's beginning 1947 accounts receivable exceeded his ending accounts receivable by $23,867.02 (R. 105), and this difference alone, if conversion of Exhibit 105 to the accrual basis had been made, would have reduced the net income reflected by that exhibit to $26,876.73 as against the $26,105.99 reported.

The $50,743.72 net income shown by Exhibit 105 reflected the allowance by the Government as deductible of $11,259.07 in expenses listed on Exhibit 103 as "Expenses Not Previously Allowed". (R. 248-250.) Notwithstanding this concession, the trial court instructed that it was for the jury to determine whether and to what extent the expenses were deductible. (R. 195-196.) The Court of Appeals approved, on the ground that the Government's

concession as to the expenses "was strictly limited to allowing them as an offset on the bank deposit method." (Op. 9-11.)[2]

In denying petitioner's motion at the close of the Government's case the court addressed Government counsel and said, among other things (R. 115-117):

> I think, Mr. Dim, however, that my doubt as to the relevancy of the so-called bank deposit method of computing net income and the so-called net worth plan has increased rather than lessened since you have introduced it.
>
> Assuming you had entered only the bank deposit method. Certainly this Court wouldn't want to find this man guilty of a felony or sustain a verdict on such a computation, or on the net worth method. You are, after all, relegated to the books and records in this case to establish the understatement of the income. * * *
>
> The difficulty I have here, even with the corroboration theory, is that the understatement in the books and records is not a matter that needs corroboration. It appears from the books and records. You don't need any other corroboration. * * * You have established there what you contend the books and records disclose. There is nothing to indicate that we have to resort to any outside source to corroborate those or there isn't anything to indicate that there are any other items that are not reflected in the books and records.
>
> As I look at it now, it seems to me that the only probative value, if it has any probative value, the

[2] In this connection the Court of Appeals quoted from the trial court's memorandum wherein it was stated, among other things, that "the testimony is silent" as to whether the petitioner had been reimbursed by Douglas for his travel and living expenses, the two major items on Exhibit 103. (Op. 10; R. 248.) This statement was in error: the petitioner testified that he had spent substantial sums for these purposes for which he had not been reimbursed. (R. 142.)

so-called net worth and so-called bank deposit, is insofar as it may tend to corroborate the understatement of the books. But then I can't escape the conclusion that there isn't any dispute over those items if you are sound. In other words, you have established them by the books and records.[3] You don't need to resort to any outside source to show the understatement. Why then should you have resort to the so-called bank deposit method to corroborate something that does not need corroboration?

* * * * * *

The Court: Your bank deposit method is necessarily based upon the theory that he was, for income tax purposes, on a cash basis.

Mr. Dim: That is correct.

The Court: Your bank method is based upon the theory that he is on a cash basis. If he is not on a cash basis you haven't any lawsuit, have you?

Mr. MacKinnon (the District Attorney): He is on the basis he filed on.

The Court: I say, however, if there is an issue of fact as to whether he is on a cash basis or an accrual basis, if the jury finds he is on an accrual basis, if that is an issue of fact, you haven't any lawsuit. * * *

As noted above, ultimately the court charged the jury that the defendant kept his books and was entitled to have his income determined according to the accrual method of accounting. (R. 193-194.)

In its instructions to the jury the trial court stated that the receipts-and-disbursements method had been admitted

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[3] The prosecution never tried to compute the petitioner's income from his books and records until after filing of the complaint, and then only as a result of their delivery by the petitioner to the district attorney's office. (R. 1, 24, 52, 66, 87, 91.) Following initial refusal of the court to receive evidence of receipts and disbursements, the Government proceeded with proof from such books and records, primarily through an accountant employed by the petitioner. (R. 47-50, 57-67.)

"solely for the purpose of establishing whatever corroboration, if any," it might afford. (R. 194.) There was no explanation of what legal significance, if any, the term "corroboration" might have in the circumstances.

The verdict was returned before December 6, 1954, the date of this Court's decision in *Holland v. United States*, 348 U. S. 121. (R. 205.) On appeal the petitioner urged that that decision required setting aside of the verdict on both of the above grounds interposed as objections to use of the Government's circumstantial method of proof in that the *Holland* case holds that, in circumstances such as those here present, a condition precedent to such use is independent evidence of a "likely source of unreported taxable income" not susceptible of direct proof (pp. 130-132, 138) and, further, that the income shown by such method must be "currently taxable income" (p. 137). The first contention was disposed of summarily with only the statement that the *Holland* decision "makes it clear" that a circumstantial method of proof "may be used even in cases where the taxpayer's books are not shown to be inadequate", followed by a quotation from the decision itself. (Op. 19.) The second contention was not discussed.

Received in evidence without objection by the petitioner was Exhibit 1, which was a filled-in return form for 1947 and bore the petitioner's name. (R. 4, 223-227.) It appeared later from testimony of the petitioner and his wife that the petitioner had never previously seen the document and did not recall until it was presented in court that he had not signed it; that he had not seen a copy until some time after October 1, 1948; that he was in Oregon at the time the document was prepared and filed in Min-

nesota; that he had no communication with any one regarding its preparation or its contents; and that his wife had never previously signed such a document for the petitioner. (R. 141-142, 167-168.) The wife testified that "My husband did not authorize me to file this return in his behalf." (R. 167.) There was no evidence contradictory of the foregoing.

The court instructed the jury that "It is not contended that she [the wife] did not have authority from defendant to sign this return, so it is conceded that the return * * * constitutes defendant's income tax return regardless of the fact that he did not sign it." (R. 199.) Counsel for the petitioner failed to take an exception to this instruction. (Op. 16.) However, in the course of preparation of the petitioner's brief in the Court of Appeals, their attention was drawn to the memorandum decision of the Tax Court in *Miller v. Commissioner,* Dock. No. 43633, decided April 29, 1955, and published in C. C. H. Tax Reporter as Dec. 20,994(M), wherein it was held that a "return" signed with the taxpayer's name by his wife is not a return at all, even though authorized by the taxpayer, and that if the taxpayer's failure to sign it is due to willful neglect, he may be assessed a penalty for failure to file a return. It appeared to counsel that if this holding was sound the petitioner could not lawfully be found guilty of the offense with which he was charged, which was (R. 1) that he willfully filed a fraudulent "return". Since the issue goes to the basic validity of the entire prosecution and therefore is a substantial one and since it could not reasonably have been anticipated, the petitioner asked the Court of Appeals to consider the issue under Rule 52 (b) of the Rules of Criminal Procedure. (Op. 15.)

The court granted the request but upheld the trial court on the grounds, first (Op. 16), that "the jury were justified in finding that the defendant filed or authorized the filing of his return" and, second (Op. 17), that "If the purported return can not be technically considered a return, it would seem that it constitutes a false statement", the making of which *United States v. Beacon Brass Co.*, 344 U. S. 43, holds may be an offense under §145 (b), the court referring at the same time, however, to *Spies v. United States*, 317 U. S. 492, which set aside a conviction under §145 (b) for the reason that no return had been filed.

REASONS FOR GRANTING THE WRIT

Question One

The issue raised by this question is whether the Government may resort to circumstantial methods of proving understatement without first offering evidence sufficient to support at least an inference that there is unreported taxable income not susceptible of direct proof, in this instance from available books and records. As we read the decision below, it holds that such preliminary proof is unnecessary. There is reason for believing that this holding is contrary to the principles laid down by this Court in the *Holland* case and is in conflict with the construction placed upon the *Holland* decision by other courts. The question, moreover, is one of unusual current importance because of the large volume of tax evasion litigation, civil as well as criminal, presently engaging the attention of the courts, and there appears to be uncertainty on the part of the profession as to how the principles of the *Holland* case are properly to be interpreted and applied.

As we read the opinion of the Court of Appeals, in the light of the circumstances here present it construes the statement in the *Holland* case (p. 132) that "the Government must be free to use all legal evidence available to it in determining whether the story told by the taxpayer's books accurately reflects his financial history" as meaning that resort may be had by the prosecution to circumstantial methods of proof under any and all circumstances, at least if application of such methods produces a larger net income than that reported. The *Holland* decision appears to lay down no such broad doctrine. After emphasizing, among other things, that the courts "must closely scrutinize" the use of such methods and exercise "great care and restraint" (pp. 125, 129), this Court there pointed out (p. 132) that the evidence in the *Holland* case warranted the conclusion "that the defendants' books were more consistent than truthful, and that many items of income had disappeared before they had even reached the recording stage" and (p. 137) that "there was ample evidence that not all the income from the hotel had been included in its books and records." Thus there was in that case what this Court called "proof of a likely source" of unrecorded and unreported income; such proof, this Court said (p. 138), "is sufficient". As summarized in the headnote: "There was independent evidence of a likely source of unreported taxable income which the jury could reasonably find to be the source of the increases in net income reflected by the circumstantial method employed by the Government."

In striking contrast, there was at bar no independent evidence of a likely source of unreported taxable income not susceptible of direct proof from available books and rec-

ords; on the contrary, there was express disclaimer of the existence of any such evidence. We think it clear, in the light of the facts here present, that the Court of Appeals has misinterpreted and misapplied this Court's decision in the *Holland* case.

Moreover, the broad construction placed on the *Holland* decision by the court below appears to be in conflict with the interpretation placed on that decision by Courts of Appeals for other circuits and also by other courts. It is said, for example, in *United States v. Adonis* (C. A. 3rd), 221 F. 2d 717, 719, that—

> under the doctrine of the Holland case, "proof of a likely source", without evidence of how much that source yielded, is sufficient additional evidence to justify the inference the government seeks to create [that the results of the circumstantial proof reflect unreported taxable income].

Likewise, *United States v. Costello* (C. A. 2nd), 221 F. 2d 668, certiorari granted October 10, 1955, states that under the *Holland* decision the circumstantial proof alone "is not enough" (p. 670) and that by way of addition this Court (p. 671)—

> is satisfied with "proof of a likely source, from which the jury could reasonably find that the net worth increases sprang". * * *

In like manner it is said in *Strauch v. United States* (C. A. 6th), 223 F. 2d 377, 381:

> The government proved by testimony independent of the statements used in evidence a consistent pattern of underreporting large amounts of income and of defendants' failure to include all of their income in their books and records. Holland v. United States, supra, 348 U. S. 139, 75 S. Ct. 127. Independent

> evidence was shown of the likely source of unreported taxable income. Holland v. United States, supra, 348 U. S. 138, 75 S. Ct. 127. * * *

A similar view of what the *Holland* case teaches has been taken by at least one district court. In *United States v. O'Malley* (E. D. Pa.), 131 F. Supp. 409, it is said (p. 413) that the *Holland* case holds that "the Government has the burden of showing a likely source of unreported taxable income". The opinion then goes on to state (p. 413):

> As to likely source of income, the Holland case posed no difficulty. The defendant there operated a hotel and bar during the prosecution year. The Government alleged that only part of the income was registered in the books and it was shown that the hotel had produced, before the defendant became owner, profits substantially in excess of those reported. * * *

It seems not unfair to say that the same understanding of what the *Holland* case holds has been indicated by the Tax Court in a memorandum opinion involving civil fraud. In *Straehley v. Commissioner,* Dock. No. 41431, decided May 6, 1955, and reported in C. C. H. Tax Court Reporter as Dec. 21,000(M), the Commissioner imposed fraud penalties measured by income computed according to the circumstantial method of proof employed in the *Holland* case. There was no evidence that the taxpayer had any income from sources not reflected either in his own records or in those of third parties with whom he did business. On this ground the court concluded:

> It is held, therefore, that respondent's resort to the increase in net worth method was not justified and

> was improper, and that his determinations of deficiencies based thereon are erroneous and cannot be sustained. * * *

It should be pointed out, however, that the *Holland* case was not cited until in the second paragraph following the paragraph from which the foregoing quotation is taken.

The widespread importance to both taxpayers and their counsel of the *Holland* decision and of such implications and limitations, if any, as are inherent in it is manifest from the volume of literature it has evoked. It is true that much of what has been written relates only indirectly to the precise issues here raised, and a substantial part is in the nature of "recent case" articles, but the volume is sufficient to demonstrate that the granting of review of the decision below would not serve merely narrow or fleeting ends. Included in the literature on the subject are the following:

28 Temple Law Quarterly 426, Net Worth and Other Indirect Methods Used in Federal Income Tax Prosecutions.

24 Cincinnati Law Review 380, The United States Supreme Court Rules on Net Worth Theory.

4 De Paul Law Review 237, Net Worth and Proof of Tax Evasion.

41 American Bar Association Journal 512, The "Net Worth" Decisions: Proof of Tax Evasion by Inference.

3 Kansas Law Review 351, The Net Worth Method in the Prosecution of Income Tax Fraud.

5 Catholic University Law Review 198, Taxation—Criminal Tax Evasion—Use of Net Worth Method —Sufficiency of Evidence.

35 Boston University Law Review 313, Taxation—Establishing Guilt of Tax Evasion—Net Worth Method.

21 Brooklyn Law Review 297, Taxation—Evasion of Income Tax—Extended Use of Net Worth Method.

32 Dicta 237, Taxation: The Use of the Net Worth Theory in Criminal Prosecution for Income Tax Evasion.

17 Georgia Bar Journal 410, Taxation—Net Worth Method of Proof of Income Tax Evasion.

1 Howard Law Journal 225, Federal Taxation—Net Worth Method of Proof—Evidence Requirements.

9 Southwestern Law Journal 366, Federal Income Tax—Criminal Prosecution for Evasion—Net Worth Theory.

2 University of California at Los Angeles Law Review 585, Federal Income Taxation: Fraud: Proving Fraud by the Net Worth Method.

4 Utah Law Review 414, The United States Supreme Court Holds Use of Net Worth Method Not Limited to Cases Where Books are Inadequate.

Question Two

It may not be asserted that this question—whether it is proper in the case of an accrual-basis taxpayer to permit proof of income on the cash basis when it is possible to make proof on the former basis—has been decided in a way either contrary to the holdings of this Court or in conflict with the decisions of other Courts of Appeals, for the reason that it was not answered at all. The question is nevertheless highly important, for the casting aside of the

question by the Court of Appeals in this instance brings into sharp focus the precautionary admonitions which this Court was at such pains to emphasize in the *Holland* case. Moreover, it is closely linked to the first question raised.

That income-tax liability is to be determined according to the taxpayer's method of accounting is basic. *Dixie Pine Prod. Co. v. Commissioner,* 320 U. S. 516, 519; *Security F. M. Co. v. Commissioner,* 321 U. S. 281, 285-286; *Healy v. Commissioner,* 345 U. S. 278, 281. No doubt the court below would readily agree that this is so; for in another recent income-tax prosecution it held that it was not error to deny permission to a cash-basis defendant to prove what his income was on the accrual basis (*Clark v. United States,* 211 F. 2d 100, 105), and presumably it would not knowingly grant to the Government a right for the purpose of securing a conviction which it denies to a defendant for the purpose of establishing innocence. Yet in effect this is precisely what the Court of Appeals has done in this instance.

In the *Holland* opinion this Court said (p. 137) that when the Government resorts to circumstantial methods of proof it must show that the results "are attributable to currently taxable income." It also warned (p. 128), having particular reference to charts taken to the jury room, that "bare figures have a way of acquiring an existence of their own, independent of the evidence which gave rise to them."

It appears that the Court of Appeals thought decision of the present question unnecessary, on the ground that "there was adequate proof of specific omissions [based on books and records] to support the jury's finding of a substantial understatement" and hence that considera-

tion of the question would be "mere academic exercise". (Op. 20-21.) This view, we submit, is a serious transgression of the precepts of the *Holland* decision.

So far as understatement based on books and records (specific omissions) is concerned, the case turned on two issues, both of which were left to the jury. The one was whether cancellation of the $10,000 loan constituted taxable income, and the second was whether the $11,259.07 in "Expenses Not Previously Allowed" was deductible. If the jury answered both of these issues favorably to the petitioner, then on the basis of specific omissions the petitioner's net income was $23,778.58, an overstatement of $2,327.41,[4] whereas on the basis of cash receipts and disbursements his net income was $40,743.72 (R. 250), an understatement of $14,637.73.

In concluding that it would be superfluous to pass on the question whether it was proper to permit proof on the cash basis, the Court of Appeals necessarily assumed that as to both these issues the jury found against the petitioner. This assumption overlooks the fact that the jury could have found, and so far as any one can or does know did find, in favor of the defendant on both these issues and nevertheless have also found, on the basis alone of cash receipts and disbursements, that there was a substantial understatement. No appellate tribunal, with the admonitions of this Court before it, should in the circumstances of this case say, certainly not with conclusive assurance, that the verdict of the jury was not returned on the latter basis. The question is not whether the jury *could* have returned such a verdict as it did, had no

[4] More accurately, the figures should be $23,379.25 and $2,726.74, respectively, for the Government conceded the deductibility also of $399.33 in additional depreciation. (R. 250; Op. 4.)

evidence been received of cash receipts and disbursements, but whether it *would* have done so.

In this respect *United States v. Burdick* (C. A. 3rd), 214 F. 2d 768, remanded, 348 U. S. 905, reaffirmed, 221 F. 2d 932, which was cited by the Court of Appeals as precedent for its non-action (Op. 20), is quite unlike the instant case. For there the court pointed out (221 F. 2d 934) that the jury could not have reached the verdict it did without finding that the omitted specific receipts there in controversy represented taxable income and that the case "pivoted" on that issue; a like statement may not be made here. Peculiarly apposite here is what recently was said in respect of the *Burdick* case in *Brown v. United States* (C. A. 6th), 224 F. 2d 845, 848:

> It may be that in a case where the issue of tax evasion may be close upon balanced direct evidence, prejudice might be perceived in the introduction of a net worth statement subject to criticism for infirmities therein. * * *

That the instant case is such a "close" case is clear by the acknowledgment of both the trial court and the Court of Appeals. The latter pointed out (Op. 18) that on the record here made "the jury could readily have arrived at a verdict for the defendant", and it indicated (Op. 14) that, like the trial court, had it sat as the trier of fact "it might have arrived at a different interpretation of the evidence".

We should think it important, not alone to the present petitioner, but to the Government and also to others, that the question be settled whether, in view of the reference in the *Holland* case to "currently taxable income", the prosecution may make circumstantial proof of income accord-

ing to a method of accounting different from that employed by the defendant when the elements of proof on the latter basis are available.

Question Three

The Commissioner of Internal Revenue has prescribed strict rules in respect of the signing of returns (Reg. 111, §29.51-2; Reg. 118, §39.51-2) and has consistently and successfully urged that meticulous compliance is prerequisite to a valid return, with the consequence that a filed "return" signed with the taxpayer's name by one who, though authorized to do so, does not hold a written power of attorney for the purpose is not in law a return at all and does not prevent imposition of a penalty for failure to file (*Miller v. Commissioner, supra*) or toll the statute of limitations against the determination of deficiencies (*Overbeck v. Commissioner,* T. C. memorandum decision, Dock. No. 46,546, decided August 31, 1955, and published in C. C. H. Tax Court Reporter as Dec. 21,214 (M)). Cf. *Lucas v. Pilliod Lumber Co.,* 281 U. S. 245, 249. See also *Spies v. United States, supra.*

We should think it of manifest importance, particularly to those charged with the administration and enforcement of our tax laws, that it be settled whether a document which the courts generally regard as not being a return for civil purposes is nevertheless a return for criminal purposes. Two Courts of Appeals have held that the enacting civil requirements should be relaxed where criminal prosecution is involved. In *United States v. Albanese* (C. A. 2d), 224 F. 2d 879, certiorari denied October 10, 1955, it was held that return-forms signed by others than

the defendant without powers of attorney were returns because the defendant, among possible other reasons (p. 882), "had given permission to the others to sign them for him." And in *Gariepy v. United States* (C. A. 6th), 220 F. 2d 252, certiorari denied October 10, 1955, it was held that unsigned return-forms should be regarded as operative returns where the defendant himself, among other things (p. 255), "had directed the transmission of the information furnished" to those who prepared the returns.

Right or wrong, the *Albanese* and *Gariepy* cases are not revolting in holding that one who knows, as evidently Albanese and Gariepy did, what is set out in the form prepared for filing in his name and who then, so knowing, asks or directs another to sign it for him or causes it to be filed without any signing, should be regarded as having filed an operative return for criminal purposes even though not for civil. But that is not this case. No one asked for or was given permission to inscribe the petitioner's name or sign it in his behalf. The subject was not even discussed, and the petitioner's wife, who signed the return, did so, not because she was given authority or was asked to do so, but because her husband was absent and, in her own words, "It was so near the deadline I suppose, it had to be signed and taken care of." (R. 141-142, 142-143, 167-168.)

CONCLUSION

This is a case which, both lower courts agree, might well have resulted on the merits in a verdict of not guilty. It raises significant questions deserving of consideration at the hands of this Court for the purpose of clarifying and settling important issues of general interest. The writ should issue.

Respectfully submitted,

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Attorneys for the Petitioner.

APPENDIX

United States Court of Appeals

FOR THE EIGHTH CIRCUIT

No. 15,262.

Edward S. Canton, Appellant,

vs.

United States of America, Appellee.

Appeal from the United States District Court for the District of Minnesota.

[October 20, 1955.]

Hayner N. Larson (Raymond A. Scallen and Oscar G. Haugland were with him on the brief), for Appellant.

Alex Dim, Assistant United States Attorney (George E. MacKinnon, United States Attorney, was with him on the brief), for Appellee.

Before SANBORN, COLLET, and VAN OOSTERHOUT, Circuit Judges.

VAN OOSTERHOUT, Circuit Judge.

The appellant, Edward S. Canton, hereinafter referred to as the defendant, was found guilty by a jury on a charge

by information of violating 26 U.S.C., § 145(b), by filing or causing to be filed a fraudulent income tax return for the year 1947. He appeals from the denial of his motion for judgment notwithstanding the verdict and from final judgment and sentence on the guilty verdict.

Defendant, who was 53 years of age at the time of the trial, is a high school graduate, and has had one year of college education and a short course at a business school. After working for various employers in the lumber industry, he established the Canton Lumber Sales Company in Minneapolis in 1930. He has been the sole proprietor of this business at all times since, except for a period of about five years ending in 1938 when his brother Paul was associated with him as a partner. At the outset the defendant acted exclusively as a salesman for lumber mills strictly on a commission basis. The bookkeeping then was simple as the mills billed and collected from the customers and paid the defendant his commission. Later his business developed into a wholesale lumber business. The lumber was still generally shipped direct to the customer, but the defendant paid the mill and he in turn billed and collected from his customers. He usually charged a customer five per cent above his cost which was the maximum mark-up permitted by the Office of Price Administration during most of the involved period. The defendant was allowed two per cent cash discount and he allowed his customers a two per cent cash discount for prompt payment.

In 1945 lumber was hard to get. Defendant was unable to supply the needs of his customers. Defendant with Baldridge, a man with mill experience, purchased a lumber mill at Drain, Oregon, which was incorporated under the name of Douglas Timber Corporation, hereinafter sometimes referred to as Douglas. Defendant secured financial

assistance for the mill purchase and operation by means of sale of stock and personal loans from many of his customers upon assurance that this would put them in a preferred position to obtain hard-to-get lumber. Baldridge died unexpectedly, so it was necessary for defendant to assume management of the lumber mill and to spend nearly all of his time in Oregon from March 1946 until October 1948 when the mill was sold. Defendant was not an experienced mill operator, and this project created many difficult financial, labor, and other problems which made heavy demands upon the defendant's time.

During defendant's absence in Oregon the bookkeeping at Minneapolis was done by his niece, Tanea Canton, since married and now Tanea Bradley. When she started working for the defendant in the fall of 1945, Tanea was 18 years of age and had recently graduated from high school where she had taken a bookkeeping course. During most of the involved period defendant's other employees in Minneapolis were two salesmen. Tanea's duties were to compute the profits, do the bookkeeping, make out bank deposit slips, type customers' invoices, and take care of some correspondence. The defendant had instructed Tanea as to how to handle the bookkeeping. She had written down the instructions which have since been lost. Tanea said that she followed the instructions to the best of her ability and that she was not aware of the fact that any profits were being concealed. The records consisted of a cash book, order books, a car journal, a customers ledger, and invoice files. The cash book was supposed to contain entries showing all profits, including wholesale profits and commissions, and all items of business expense. The only record turned over to and used by Mr. Holl, a lumber dealer who prepared the income tax return in question and defendant's returns for many prior years, was the cash book.

Further facts will be discussed hereinafter.

Defendant in his brief thus states the questions presented for review:

"The return filed for the defendant, a wholesale lumber dealer, reported a net income of $26,105.99. Concededly omitted from gross income were the following items and amounts:

(a) Special 5% discount allowed on purchases from Douglas Timber Corporation	$ 5,531.03
(b) Offset of 2% discounts for prompt payment granted to and allowed by the defendant	488.23
(c) An interest check received from Douglas	1,001.39
(d) Direct sales commissions represented by two checks received from Douglas	1,911.01
Total	$ 8,931.66

"The omissions represented by items (a) and (b) are reflected in detail in the defendant's books and records. Those represented by items (c) and (d) are reflected in detail in the Douglas books and records, for which the defendant was responsible.

"Not deducted on the defendant's return were the following items allowed as deductions by the Government's agents:

(e) Depreciation (Ex. 105, R. 250)	$ 399.33
(f) Miscellaneous expenses, principally living and travel expenses on the West Coast (Ex. 103, R. 248)	11,259.07
Total	$11,658.40

"Assuming that there were no omissions from gross income other than items (a) to (d) (and, as will be seen, there were no such other omissions), the defendant's return overstated his net income by $2,726.74 unless the cancella-

tion by the defendant's brother of a $10,000 loan to the defendant represented income taxable to the defendant.

"The principal questions are—

"(1) Whether there is substantial competent evidence from which it could be found beyond a reasonable doubt that cancellation of the $10,000 loan was taxable income.

"(2) Whether, if question (1) should be answered in the affirmative, there is substantial evidence from which it could be found beyond a reasonable doubt that the resulting understatement in net income was due to an intent to evade.

"(3) Whether, if both question (1) and question (2) should be answered in the affirmative, there is substantial evidence of such an overt act reflecting willfulness as is required by *Spies* v. *United States*, 317 U.S. 492, and, in this connection, whether, if there is such evidence, the court erred in refusing to instruct the jury in the detail set out in the defendant's first requested instruction.

"If questions (1), (2) and (3) should all be answered in the affirmative, then

"(4) Whether the court erred in permitting resort to a circumstantial method of proving understatement in net income, there being no evidence, but on the contrary a concession, that the defendant had no additional income from the same sources as items (a) to (d) and no income from other or undisclosed sources; and, moreover, if the court did not so err, whether the circumstantial method so permitted did in fact furnish a sufficient basis for a finding beyond a reasonable doubt that there was an understatement in net income, particularly since such method purported to reflect income according to the cash method of accounting whereas the court instructed the jury (R. 193) that the defendant's business income was determinable only according to the accrual method of accounting, and since such circumstantial method in addition treated as income substantial items which the court instructed the jury did not constitute income under either method of accounting (R. 199).

"(5) Whether the court erred in instructing the jury in such a way as to permit the jury to treat as nondeductible the items (e) and (f) above, particularly the latter, which were allowed as deductions by the Government's agents.

"(6) Whether the prosecuting attorney indulged in unwarranted statements and remarks in his arguments to the jury, to the defendant's substantial prejudice."

We proceed to the consideration of the issues raised by the defendant.

(1) Defendant upon his urgent request obtained a $10,000 loan in January 1947 from his brother Paul who was engaged in the retail lumber business at Watson, Minnesota. The loan is shown in defendant's customers ledger. Paul, in a letter to defendant dated July 7, 1947, writes:

"Dear Ed:

"Last January I turned over to your firm the sum of ten thousand ($10,000.00) dollars. I think you have been carrying this amount on your books (and statements) as cash advanced against future purchases.

"In view of the fact that I agreed to share with you a percentage of my net operating profit, for acting as supplier and purchaser of hard-to-get merchandise, I have charged the sum advanced to you to the cost of such merchandise. The sum of ten thousand dollars is therefor tendered to you in lieu of any expected profit percentage. As far as I am concerned, you are authorized to remove the above mentioned sum and entry from your records of advance payments or accounts payable.

Yours truly,

Paul J. Canton"

Defendant admits receiving the above letter and entering on his customers ledger a $10,000 charge to offset the $10,000 credit, and also making the following notation:

"July 7, 1947, to services rendered per letter from Paul J. Canton, $10,000." Defendant insists that the cancellation of the foregoing $10,000 loan constitutes a gift exempt from tax under section 22(b) (3) of the Internal Revenue Code, and in support cites *Helvering* v. *American Dental Co.*, 318 U.S. 322, and *Commissioner v. Jacobson*, 336 U.S. 28. In the *American Dental* case, *supra*, the Court thus defines "gifts:"

"* * * Its plain meaning in its present setting denotes, it seems to us, the receipt of financial advantages gratuitously."

In the *Jacobson* case, *supra*, the Supreme Court, in reversing the Court of Appeals, held that the discount at which a solvent debtor purchased bonds upon which he was liable was income rather than a gift. Justices Reed and Douglas dissented on the basis of the *American Dental* case. Justice Rutledge, specially concurring, expressed the opinion that the result was in conflict with the *American Dental* case. The majority distinguished the *American Dental* case and stated (p. 51):

"The situation in each transaction is a factual one. It turns upon whether the transaction is in fact a transfer of something for the best price available or is a transfer or release of only a part of a claim for cash and of the balance 'for nothing.' "

In *United States v. Burdick*, 3 Cir., 214 F. 2d 768, remanded 348 U.S. 905, reaffirmed 221 F. 2d 932, the issue we are now considering is quite fully discussed. At page 771 of 214 F. 2d we find the following:

"As we held in Smith v. Manning, 1951, 189 F. 2d 345, 348 whether the receipts are gifts is primarily a question of fact to be resolved upon the peculiar circumstances of the case; the mere fact that the payments were voluntary does not establish them as gifts; if the payments were made

without a donative intent and as compensation for services they constitute taxable income. * * *"

The fact issue of whether the cancellation resulted in a gift or taxable income was submitted to the jury under proper instructions. The record shows that the defendant did in fact ship considerable scarce lumber to his brother Paul. On cross-examination defendant testified as follows:

Mr. Dim: "But Paul was very grateful to you for getting lumber for him all that time?"

The Witness: "Yes."

And at another point:

Q. "Isn't it a fact that the loan was cancelled in July because it was for procurement of lumber for Paul Canton?"

A. "Yes."

And on further cross-examination:

Q. "Now with reference to the Paul Canton $10,000 matter for the year 1947, during that same question and answer period of October 17, 1951, didn't you state that as long as your brother, Paul, treated it as a procurement expense that you were willing to accept it as such?"

A. "If I said that it was an error of legal knowledge."

There is also testimony of three Government agents that during the course of the investigation the defendant told them in substance that the $10,000 note cancellation was income and should have been reported. Defendant insists that this admission to the agents is an admission after the fact and as such should be corroborated. The contention in this respect is supported by *Smith* v. *United States*, 348 U.S. 147, and *Opper* v. *United States*, 348 U.S. 84. Here, there is ample corroboration. Defendant makes the further claim that the admission to the agents is one of law and not one of fact. This contention was not raised before the trial

court by objection to testimony or motion to strike or in any other manner. Consequently, we are not required to consider it. In any event there is ample evidence exclusive of the admission to the agents to support the verdict.

We have not detailed all of the evidence bearing upon the gift issue. There is, of course, some evidence on this issue favorable to the defendant. The defendant testified that he made no special concessions to Paul in the delivery of lumber, that he performed no services for him for which he was not compensated. In view of the verdict the evidence must be considered in the light most favorable to the Government. So considered the record would support a finding by the jury that the cancellation of the $10,000 loan was for services rendered and hence taxable income.

As heretofore noted defendant conceded omissions of income totalling $8,931.66, which total does not include the $10,000 debt cancellation. From this he sought to deduct $399.33 depreciation about which there is no serious controversy, and $11,259.07 in miscellaneous expenses of which $7,978.55 was for living expenses in Oregon, and thus establish that he had not understated his income. The Government denies that the defendant is entitled to a deduction for the Oregon living expenses. Such expenses appear in Government's Exhibit 103 and were part of the Government's proof in establishing income by the bank deposit method. The testimony of Aas, the Government agent who made the bank deposit computation, is:

"Referring to Exhibit 103 'Expenses not previously allowed for the year 1947', the item of $6,920.82 shown as living expenses at Drain, Oregon, and the item of $1,057.73 shown as business expenses were transcribed by me from information in Mr. Diracles' [defendant's accountant]

records and I allowed these amounts for our bank deposit method. I did not verify them."

The trial court in ruling upon the defendant's motion for acquittal or for a new trial stated:

"* * * But merely because the Government gave the defendant the benefit of these deductions from gross bank deposits in computing net income by the bank deposit method, that fact does not necessarily establish such expenditures as deductible in determining defendant's net income from his books and records. Defendant recognized in his request for instructions to the jury that such items were deductible only to the extent that he had not been reimbursed for such outlays from other sources. He made no record of these expenses in his books and records. The testimony is silent as to whether or not he received any reimbursement from the Douglas Timber Company. And moreover, the evidence is impelling that Canton's stay on the West Coast was primarily in the interest and in behalf of the Douglas Timber Company. True, he was promoting the Douglas Timber Company's activities so that the Canton Lumber Sales would have a source for lumber in its wholesale business. The indisputable fact nevertheless remains that the Douglas Company was an independent corporation and not a subsidiary or adjunct of the Canton Lumber Sales. It was a producer and manufacturer of lumber in Oregon. Canton Lumber Sales was a wholesaler of lumber in Minneapolis. To the extent, if any, that any portion of these expenses in light of the evidence constituted a permissible deduction for Canton as an individual in computing his 1947 income tax was a matter of considerable speculation and uncertainty. However, the Court permitted the jury to determine that question notwithstanding."

We agree with the trial court that the defendant was not entitled to these unclaimed deductions as a matter of law. It seems obvious that the Government's concession as to the living expenses was strictly limited to allowing them as an offset on the bank deposit method. The trial court vio-

lated no legal rights of the defendant in submitting to the jury the question of the living expenses to be allowed the defendant.

We are convinced that the evidence of the specific omissions alone was sufficient to warrant a finding by the jury that the defendant substantially understated his income in the 1947 return filed.

(2) Is there substantial evidence that defendant's understatement was attributable to an intent to evade taxes? It is clear that the record here would support a finding that substantial items of income were not reported. Mr. Holl had since 1933 prepared defendant's income tax returns, obtaining all information for such returns from defendant's cash book. The jury could find that the defendant knew that his tax expert did consider only the items entered in the cash book in preparing the returns. In such a situation, where the defendant knew that any other records he might have were not being considered in making the return, the fact that he might have more complete records in other books or files would not be particularly material. In setting out profits from sales in the cash book, $488.23 in profits created by customers not taking their cash discounts is concededly omitted. Defendant also admits that he specifically instructed his bookkeeper to ignore the cash discount allowed defendant and that allowed the customers in computing profits. His explanation is that this was so handled to simplify and expedite the bookkeeping, and that a check made by him a number of years before had shown that the profit and loss occasioned by ignoring cash discounts would offset. When a car of lumber was billed to defendant at $1,000, he would deduct two per cent and remit $980 to the mill. He would then add his five per cent mark-up to the original $1,000, and bill his customer for $1,050. The two per cent discount on this would be $21. If the

defendant and the customer each took the discount, the profit would be the difference between the customer's net cost of $1,029 less defendant's net cost of $980, or a total of $49. In entering the profit on such a sale, the defendant disregarded all discounts, and entered as a profit the difference between $1,050 and $1,000 or $50. Thus, where each took the discount, the result was an overstatement of profit of $1. The defendant always took his discount. If the customer overlooked his discount, the defendant would collect $1,050, and his profit would be the difference between that figure and his net cost of $980 or $70. In such a situation there would be an understatement of profit of $20. There is evidence from which the jury could find that due to material scarcity the defendant encouraged some of his customers to waive their cash discounts and that quite a number of customers did so. In 1946 the omitted income resulting from not considering the cash discounts amounted to $5,124.47.

After defendant acquired Douglas he received a five per cent discount on all his purchases, this being in addition to the usual five per cent mark-up and two per cent discount previously received. This additional five per cent discount is not reflected in his cash book and was not considered in computing and entering the profits in his cash book. Such omission resulted in a $5,531.03 understatement of income in 1947, and in 1946 resulted in a $14,599.97 understatement. The defendant admitted that he gave his bookkeeper no specific instructions as to how to enter this five per cent mill discount. While defendant spent much of his time in Oregon, he made a number of trips to Minneapolis in 1946 and 1947. He was continually pressed for money, and it does not seem unreasonable to suppose that he was interested in his profit records. He knew that his bookkeeper was young and inexperienced, and that none of the other

employees in Minneapolis was in a position to supervise the bookkeeping or offer any help. During this period he personally made the entry in connection with the Paul Canton cancellation.

$1,911.01 of Commissions and interest in the amount of $1,001.39 were not entered in the cash book or reflected in the 1947 return. Defendant's explanation is that he sent either his checks or at least the vouchers in cases where he needed to cash the checks to his office. However, he does not claim that he gave any specific directions that these items were to be entered in the cash book, or as to how they were to be handled. Defendant in his explanation of the foregoing omissions states that he was unable to give proper attention to his Minneapolis business because of his absence from Minneapolis and the terrific load placed upon him at Douglas.

Wiseley v. *Commissioner*, 6 Cir., 185 F. 2d 263, and *Lewis* v. *Commissioner*, Docket No. 37335, decided by the Tax Court in April 1955, lend some support to defendant's contention that his preoccupation with other duties may negative willful or wrongful intent in failing to report his full income. Both of these cases were civil fraud cases, and in each the court concluded the fraud penalty should not be imposed. We agree with the court's statement in the *Wiseley* case to the effect that the fact that defendant was personally busy to the point of distraction is a vitally material factor in determining the issue of fraudulent intent. From the report of the *Wiseley* case it would appear that the defendant on his own initiative, before investigation, became aware of his understatement and employed auditors and filed amended returns. In any event we believe that each case must be determined upon its own facts. It is not impossible for an extremely busy person to be guilty of fraudulent conduct. The record of defendant's business

pressure was before the jury for such consideration as they thought it was entitled to. The jury was specifically told that to convict they must find that the defendant willfully and knowingly attempted to evade the tax. The trial judge who presided over this trial and had an opportunity to hear and observe all the witnesses, in his memorandum opinion not officially reported, stated:

"My sustained conviction is that there was a question for the jury as to whether there was an understatement by defendant of his 1947 income tax. The more difficult question is whether the evidence beyond a reasonable doubt sustained an intent to evade. On a motion for judgment of acquittal, the Court must take the view of the evidence and the inferences to be drawn therefrom which is most favorable to the Government, and although the Court might have arrived at a different interpretation of the evidence as to intent than is reflected in the jury's verdict, I cannot say that reasonable minds might not have concluded in considering all the evidence, direct and circumstantial, that defendant's guilt had been proven beyond a reasonable doubt. The Court was meticulously careful to surround the defendant with every protection to which he was entitled under the law, and particular emphasis was placed upon the burden which rested upon the Government with reference to intent."

We agree with and adopt the foregoing statement.

(3) The defendant next contends that even if the Government has established a substantial understatement with intent to evade, the conviction can not be sustained because of failure to prove beyond a reasonable doubt an overt act reflecting willfulness. In supplement to the defendant's brief it is stated that the defendant did not sign the 1947 return and that consequently the instrument purporting to be a return is not a return at all. He relies upon *Miller* v. *Commissioner*, Docket No. 43633, decided by the Tax Court on April 29, 1955. Defendant's counsel contend that

they and the defendant overlooked the fact that the defendant had not signed the return until the return was produced at the trial, and that they were caught by surprise and overlooked legal implications arising from this situation. They ask that we note plain error pursuant to Rule 52(b) of the Rules of Criminal Procedure.

The factual situation is that the 1947 return was signed in defendant's name by his wife. The return is dated March 15, 1948. There is no express evidence of any direct authorization for the wife to sign the return, nor is there direct evidence to show that she was not authorized to do so. The wife was authorized to sign checks drawn on the defendant's account. Mrs. Canton testified that Mr. Holl, who prepared the 1947 return, came to the house for the cash book, and later came back to her with the completed return. There is nothing to show the wife arranged with Holl to prepare the return, so it would seem fair to assume that Holl did so either upon the request of defendant or as the result of the long-standing arrangement that Holl was to prepare defendant's returns. Defendant in his numerous visits with the investigators never denied signing or filing the return. The 1946 return was signed by Tanea Canton under similar circumstances.

A contention similar to that made by the defendant was made in *Gariepy* v. *United States,* 6 Cir., 220 F. 2d 252. There the questioned returns were not signed by the taxpayer but were prepared by a tax service from information furnished by the defendant and his employees. This problem is rather fully discussed, the court saying in part (pp. 259-260):

"Appellant argues that the 'purported' returns did not constitute income tax returns under the law; that the filing of the unsigned documents did not constitute the commis-

sion of an affirmative act requisite to sustain conviction under section 145(b). We think this contention runs contrary to the holding of this court in *Emmich* v. *United States*, 6 Cir., 298 F. 5, 9, where it was said: 'The real character of the offense lies, not in the failure to file a return, or in the filing of a false return, but rather in the attempt to defraud the government by evading the tax.' The specious contention of appellant comes rather late. At the trial, he did not deny that the documents filed with the Collector of Internal Revenue on his behalf were in fact income tax returns. * * *"

See also *United States* v. *Albanese*, 2 Cir., 224 F. 2d 879, 882.

In this case the court instructed the jury:

"It appears that Mrs. Canton signed the 1947 income tax return. She signed her husband's name. It is not contended that she did not have authority from defendant to sign this return, so it is conceded that the return, Government's Exhibit 1, constitutes defendant's income tax return regardless of the fact that he did not sign it. However, the fact that he was not present when the income tax return was prepared by Mr. Holl, and that he was not present when his wife signed it, is a matter that you may give due consideration to insofar as it may bear upon the question of his alleged intent to wilfully and intentionally commit the offense charged in this information."

Defendant did not except to this instruction. Although the defendant requested certain instructions, he made no request for any instruction on the significance of his failure to sign the return. Under the record here made the jury were justified in finding that the defendant filed or authorized the filing of his return. The filing of the fraudulent return constitutes the required affirmative or overt act. In *Cave* v. *United States*, 8 Cir., 159 F. 2d 463, 467, this court states:

"* * * The crime denounced by §145(b) of willfully attempting to defeat or evade the tax is complete when the

taxpayer willfully and knowingly files a false and fraudulent return with intent to defeat or evade any part of the tax due the United States. *Guzik* v. *United States,* 7 Cir., 54 F. 2d 618, 619, certiorari denied 285 U. S. 545, 52 S. Ct. 395, 76 L. Ed. 937; *Bowles* v. *United States,* 4 Cir., 73 F. 2d 772, 774."

If the purported return can not be technically considered a return, it would seem that it constitutes a false statement. A willful attempt to evade taxes by making a false statement violates section 145(b). *United States* v. *Beacon Brass Co.,* 344 U. S. 43. In *Spies* v. *United States,* 317 U. S. 492, relied on by defendant, there was a failure to file a return and pay the tax. The Court holds that these omissions alone would not constitute the 145(b) felony. The Court then goes on to say (p. 499):

"* * * Willful but passive neglect of the statutory duty may constitute the lesser offense, but to combine with it a willful and positive attempt to evade tax in any manner or to defeat it by any means lifts the offense to the degree of felony.

"Congress did not define or limit the methods by which a willful attempt to defeat and evade might be accomplished and perhaps did not define lest its effort to do so result in some unexpected limitation. Nor would we by definition constrict the scope of the Congressional provision that it may be accomplished 'in any manner.' By way of illustration, and not by way of limitation, we would think affirmative willful attempt may be inferred from conduct such as keeping a double set of books, making false entries or alterations, or false invoices or documents, destruction of books or records, concealment of assets or covering up sources of income, handling of one's affairs to avoid making the records usual in transactions of the kind, and any con-

duct, the likely effect of which would be to mislead or to conceal. * * *"

See also *Hoyer* v. *United States,* 8 Cir., 223 F. 2d 134; *Banks* v. *United States,* 8 Cir., 204 F. 2d 666, remanded 348 U. S. 905, reaffirmed, 223 F. 2d 884. In *Holland* v. *United States,* 348 U. S. 121, at p. 139, the Court said:

"A final element necessary for conviction is willfulness. The petitioners contend that willfulness 'involves a specific intent which must be proven by independent evidence and which cannot be inferred from the mere understatement of income.' This is a fair statement of the rule. Here, however, there was evidence of a consistent pattern of underreporting large amounts of income, and of the failure on petitioners' part to include all of their income in their books and records. Since, on proper submission, the jury could have found that these acts supported an inference of willfulness, their verdict must stand. *Spies* v. *United States, supra,* at 499-500."

Under the record in this case the jury could find a consistent pattern in failing to record and report the profits arising from the two per cent discount situation, the additional five per cent mill discount, and commissions, and also the similar omissions that occurred in 1946. Defendant's accountant admitted that the understatement of income for 1946 was $29,927.20. While on the record here made a jury could readily have arrived at a verdict for the defendant, viewing the evidence in the light most favorable to the Government as we are required to do, we can not say that the verdict is without evidentiary support. The motion made at the close of the evidence and defendant's motion for judgment notwithstanding the verdict were both properly overruled.

(4) Defendant next contends that the court erred in permitting the Government to resort to circumstantial methods of proving understatement of net income. This case was tried before the Supreme Court decided *Holland* v. *United States, supra.* The Holland decision makes it clear that the net worth method may be used even in cases where the taxpayer's books are not shown to be inadequate, the Court stating (348 U. S. at pp. 131-132):

"* * * Petitioners' accounting system was appropriate for their business purposes; and, admittedly, the Government did not detect any specific false entries therein. Nevertheless, if we believe the Government's evidence, as the jury did, we must conclude that the defendants' books were more consistent than truthful, and that many items of income had disappeared before they had even reached the recording stage. Certainly Congress never intended to make § 41 a set of blinders which prevents the Government from looking beyond the selfserving declarations in a taxpayer's books. 'The United States has relied for the collection of its income tax largely upon the taxpayer's own disclosures . . . . This system can function successfully only if those within and near taxable income keep and render true accounts.' *Spies* v. *United States,* 317 U. S., at 495. To protect the revenue from those who do not 'render true accounts,' the Government must be free to use all legal evidence available to it in determining whether the story told by the taxpayer's books accurately reflects his financial history."

Defendant contends that in any event the circumstantial methods of proof here used do not establish an understatement of net income. The defendant's return listed net income of $26,105.99. Admitted specific omissions total $8,-931.66, to which the jury would be justified in adding the

$10,000 Paul Canton item, making a total taxable income of $45,037.65, from which the jury was authorized to deduct such part of the $11,658.40 in miscellaneous expenses as they considered allowable under the court's instructions. On the bank deposit method, including the Paul Canton item, Government Exhibit 105 shows net income of $50,-743.72, and Exhibit 56 purports to show an increase in net worth of $29,449.53. Authenticity of these computations is contested by defendant. As to the bank deposit method there is much confusion as to whether the defendant's reports were on the cash or accrual basis. Mr. Holl who prepared the returns thought that he was preparing them on the cash basis, and some of the earlier returns showed on their face that the reports were on the cash basis, and the evidence is that the defendant was never given permission to change from a cash to an accrual basis. Likewise, there is considerable confusion and disagreement as to whether defendant's books were kept on the cash or accrual basis. The court in its instructions adopted the defendant's theory, and instructed that the defendant's books were kept on the accrual basis. In *United States* v. *Burdick, supra,* at pp. 933, 934, the court said:

"We are of the opinion that the conviction under review is fully sustainable without resort to the net worth theory. This being the case, it would constitute a mere academic exercise to reconsider the net worth features of this appeal in the light of the authoritative guidance furnished by the Supreme Court with respect to net worth prosecutions.

* * *

"It is apparent therefore, that the defendant was convicted for wilfully failing to report approximately $14,500 as taxable income. The receipt of these amounts was ad-

mitted. Their taxability was established by overwhelming evidence. Accordingly, the net worth computations introduced at the trial are without relevance to this appeal."

Similarly, in our present case we believe that the Government has established a case on the specific omissions admitted and proved, and that there was adequate proof of specific omissions to support the jury's finding of a substantial understatement.

(5) Under the record in this case we do not believe the defendant was as a matter of law entitled to deductions from gross income which the Government conceded were deductible for the purposes of their bank deposit method of proof. Our basis for reaching this conclusion is set out in division (1) of this opinion.

(6) Defendant finally contends that he was substantially prejudiced by the Government's arguments to the jury. To set out the argument objected to and to discuss the evidence upon which it was based would unduly extend this opinion without serving any useful purpose. In general it is charged that the Government counsel misinterpreted the evidence relative to instructions given by defendant to his bookkeeper, that counsel drew conclusions not supported by evidence from the bank deposit exhibits, and that improper allusion was made to defendant's net worth appearing in the net worth statement. Objections were made to the argument that the trial court did not sustain the objections but noted exceptions, and in some instances told the jury that if a misstatement had been made the jury should disregard it. The trial court overruled the motion for a new trial which included the objections to the argument we are now considering. We have examined the arguments as a whole in the light of the evidence and find no prejudicial error.

The consideration of the whole record convinces us that the defendant had a fair trial. The court's instructions fairly submitted the issues to the jury. The trial court has committed no prejudicial error.

The judgment appealed from is affirmed.

A true copy.

Attest:

Clerk, U. S. Court of Appeals, Eighth Circuit.

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CITATIONS

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App. 1; 226 F. 2d 313). The petition for a writ of certiorari was filed on December 12, 1955. The jurisdiction of this Court is invoked under 28 U. S. C., Section 1254 (1).

QUESTIONS PRESENTED

1. Whether the trial court committed reversible error in admitting into evidence a reconstruction of petitioner's income based upon deposits into and disbursements from his bank accounts, where substantial unreported income was proved by direct evidence.

2. Whether taxpayer's conviction for wilfully attempting to evade income taxes by filing and causing to be filed a false and fraudulent return is vitiated by the fact that his wife signed his name to the return.

STATUTE INVOLVED

Internal Revenue Code of 1939:

SEC. 145. PENALTIES.

* * * * *

(b) *Failure to Collect and Pay Over Tax, or Attempt to Defeat or Evade Tax.*— Any person required under this chapter to collect, account for, and pay over any tax imposed by this chapter, who willfully fails to collect or truthfully account for and pay over such tax, and any person who willfully attempts in any manner to evade or defeat any tax imposed by this chapter or the payment thereof, shall, in addition to other penalties provided by law, be

guilty of a felony and, upon conviction thereof, be fined not more than $10,000, or imprisoned for not more than five years, or both, together with the costs of prosecution.

* * * * *

(26 U. S. C. 1952 ed., Sec. 145.)

STATEMENT

On April 16, 1954, an information[2] was filed against petitioner in the United States District Court for the District of Minnesota, charging him with wilful attempted evasion of his income tax for the year 1947 in violation of Section 145 (b) of the Internal Revenue Code of 1939. The information alleged that he filed and caused to be filed a false return wherein he stated that his income for 1947 was $26,105.99 and the tax thereon $8,861.15 when he knew that his net income was $56,143.86 and the tax thereon $28,075.25 (R. 1). After a jury trial lasting eleven days, petitioner was found guilty as charged (R. 205). On January 4, 1955, he was fined $3,500 and placed on probation for two years (R. 213). The Court of Appeals affirmed (Pet. App. 1–22).

The evidence to support the verdict may be summarized as follows:

Petitioner, a wholesale lumber dealer, has been engaged for many years in business in Minneapolis, Minnesota, as sole proprietor of the Canton

[2] Petitioner waived prosecution by indictment. (R. 2.)

considered the so-called "Cash Book" (from which the return was prepared) worthless almost in its entirety (R. 63, 79, 91, 96, 133–134, Supp. R. 11). At the trial, the Government proved by direct evidence that in his 1947 income tax return petitioner failed to report $18,931.66 of income, consisting of the following items:

5% mill discounts received by petitioner from Douglas Timber Corporation on his own purchases (R. 78, 96)	$5,531.03
Excess of 2% cash discounts received over those granted to customers (R. 65, 110)	488.23
Interest income received from Douglas Timber Corporation (R. 88, 96)	1,001.39
5% brokerage commission received by petitioner on sales by Douglas Timber Corporation to others (R. 79, 96)	1,911.01
Amount received by petitioner from Paul J. Canton for his services in obtaining "hard-to-get merchandise" [4]	10,000.00
Total	18,931.66

[4] In January, 1947, petitioner received $10,000 as a loan from his brother, Paul J. Canton. By letter dated July 7, 1947, Paul J. Canton referred to the loan and also to an earlier agreement whereby petitioner was to receive a percentage of Paul J. Canton's net operating profit in exchange for petitioner's obtaining hard-to-get merchandise. The letter stated that Paul J. Canton had charged the $10,000 sum so advanced to the cost of merchandise and offered the amount to petitioner "in lieu of any expected profit percentage." (Ex. 21–A, R. 20, 239.) In his own handwriting (R. 20, 140) petitioner made an entry in the books writing off the loan with the notation "July 7, 1947, For Services Rendered per letter from Paul J. Canton, $10,000" (Govt. Ex. 19–A, R. 20, 237).

The Government also put in evidence a reconstruction of petitioner's income based upon deposits into and disbursements from his bank accounts. This computation purported to show a corrected net income for 1947 of $50,743.72

(Govt. Ex. 105, R. 249–250), reflecting an understatement of $24,637.73, as compared with the $18,931.66 understatement proved by direct evidence of specific omissions. Since petitioner's books were kept on the accrual method (R. 49, 63, 66, 105, 147), the computations based upon banking transactions were of dubious value (R. 105–106) and the court so charged the jury (R. 193–194, 199–200).

On the issue of wilfulness, it was shown that petitioner personally made the book entry acknowledging his acceptance of his brother's offer to convert the $10,000 loan into an income item (R. 20, 140, 239). He did not make any corresponding entry in the so-called cash book from which his income tax return was prepared (R. 152; Supp. R. 97, 99). He admitted to the agents that the $10,000 item was income which he should have reported in 1947, but at the trial he testified that the $10,000 was not for services rendered (R. 87, 140). It was also shown (R. 61) and admitted (Supp. R. 40) that petitioner's return for the previous year, 1946, understated his income in the amount of $29,927.20, and that there were substantial understatements for certain years prior to 1945 (Govt. Ex. 45, Supp. R. 149, 161).

The Court of Appeals held (Pet. App. 19–21) that there was "adequate proof of specific omissions to support the jury's finding of a substantial understatement" and therefore found no

merit in petitioner's contention that "the circumstantial methods of proof here used do not establish an understatement of net income" (Pet. App. 19).

ARGUMENT

1. Petitioner contends (Pet. 13–22) that the trial court committed reversible error in admitting evidence of the deposits into and disbursements from his bank accounts purporting to show unreported income, (a) because there was no showing of unreported income not susceptible of direct proof and hence the Government should not have been permitted to resort to circumstantial evidence; and (b) because the computations (which were made on the basis of cash receipts and disbursements) produced a result not properly comparable with his recorded and reported income (which was computed on the basis of an accrual method of accounting), and therefore operated to his prejudice.

(a) The contention (Pet. 13–18) that the Government may not use circumstantial evidence of tax evasion without first showing that there is "unreported taxable income not susceptible of direct proof" (Pet. 13) is plainly without merit. In the first place, as we shall show (*infra*, pp. 11–12) the trial court drastically limited the use to which the jury might put the computations based on banking transactions (R. 194, 199–200) and correctly submitted this case as one depending on direct proof of omitted income (*supra*, pp.

5–7). Moreover, this Court recently rejected a similar contention in *Holland* v. *United States,* 348 U. S. 121, 131–132, in the following language:

> Petitioners' accounting system was appropriate for their business purposes; and, admittedly, the Government did not detect any specific false entries therein. Nevertheless, if we believe the Government's evidence, as the jury did, we must conclude that the defendants' books were more consistent than truthful, and that many items of income had disappeared before they had even reached the recording stage. Certainly Congress never intended to make § 41 [Title 26, U. S. C.] a set of blinders which prevents the Government from looking beyond the self-serving declarations in a taxpayer's books * * * To protect the revenue from those who do not "render true accounts", the Government must be free to use all legal evidence available to it in determining whether the story told by the taxpayer's books accurately reflects his financial history.

If this is the rule in a case where the "Government did not detect any specific false entries" in the taxpayer's books, and relied wholly upon circumstantial evidence, *a fortiori,* it is the rule where, as here (*supra,* pp. 5–6), the books failed to reflect numerous items and incorrectly reflected a large number of other entries, and where the circumstantial evidence is purely subsidiary to the direct proof.

The cases cited by petitioner (Pet. 15–16) which construe the requirement laid down in the *Holland* case that there must be evidence of a "likely source, from which the jury could reasonably find that the net worth increases sprang" (348 U. S. at 138) are of no help to him. Here the obvious "likely source" of unreported income is petitioner's lumber business, the Canton Lumber Sales Company. The case of *Straehley* v. *Commissioner,* Tax Court Dec. 21,000 (M), decided May 6, 1955, 1955 C. C. H. Fed. Tax Reporter, ¶7500 (Pet. 16–17), is plainly distinguishable on the facts, for in that case the court found that the income of the taxpayer (a physician) from his profession was correctly recorded and reported.

(b) Petitioner also contends (Pet. 18–22) that the admission of evidence as to petitioner's banking transactions was prejudicial in that it reflected an amount of income computed on a method of accounting different from that employed by petitioner. Since petitioner kept his books on the accrual method of accounting (R. 49, 63, 66, 105, 147, 193) it is apparent that the reconstruction of income from bank deposits and disbursements (Govt. Ex. 105, R. 249–250 and underlying exhibits), which contemplate a cash receipts and disbursements basis, would not produce a net income figure truly comparable with that appearing on petitioner's tax return (Govt. Ex. 1,

R. 223–227).[5] The trial court clearly recognized that a conviction could not rest on such evidence alone (R. 115), and, in summing up the evidence for the jury, made it clear that the Government relied upon the specific omissions (R. 183–186, 188–190, 191, 194–195, 197–198). Strictly limiting the use to which the bank deposits evidence was to be put, the court charged the jury as follows (R. 194):

> In other words, although it is conceded that there were omissions of profits and income in the 1947 cash book, the computation of omitted items may be determined either from the books and records themselves or from other specific sources. That is, the Government in supporting its claim of tax deficiency relies primarily upon the

[5] It is true, as petitioner contends (Pet. 8) that in converting the figures from the cash to the accrual method the decrease in accounts receivable "alone * * * would have reduced the net income reflected by" Exhibit 105 to roughly the amount reported on the return, $26,105.99. However, it would be manifestly improper to reconcile for this item only. Other differences that would have to be accounted for are the $11,681.32 increase in accounts payable and the $20,265.73 decrease in "Notes payable on assigned invoices" (Govt. Ex. 56, R. 242). (See *supra*, p. 4, fn. 3.) The resultant of these changes would be a decrease in net income from $50,743.72 computed on the straight bank deposits (cash) method (Govt. Ex. 105, R. 249–250) to $35,461.11 computed on the adjusted bank deposits (accrual) method. The latter figure (which was never before the jury) compares with the corrected net income of $46,222.84 proved by direct evidence (Govt. Ex. 109, R. 252).

> omission of the so-called 5% commissions, direct and indirect, received from Douglas Timber Company, the $10,000 received from Paul Canton, the $1,001.39 received as interest from the Douglas Timber Company, and the $488 item allegedly received by way of 2% discounts not taken by defendant's customers. There may be other items upon which the Government relies, but these are the principal items which go into the alleged understatement.
>
> The so-called bank deposit method and the exhibit designated as computed net income on the net income (sic) for 1947 is admitted in evidence *solely for the purpose of establishing whatver corroboration, if any, such testimony and exhibits may afford* in establishing the alleged understatement of defendant's 1947 income as noted above. * * * [Emphasis added.]

The trial judge correctly charged that petitioner reported his income on the accrual method (R. 193), and at a later point in the charge further qualified and minimized the importance of the computations based on banking transactions (R. 199–200). Significantly, petitioner did not object to any of these instructions. Moreover, both sides recognized in their arguments to the jury the minor role played by the bank deposits. Emphasis was on the specific items of unreported income and the question of whether they were wilfully omitted from the return (Supp. R. 12–23, 29–33, 35–52), and discussion of the bank deposits

aspect of the case was relatively brief (Supp. R. 23–26, 33–34). In short, the matter was submitted to the jury by court and counsel as a direct evidence case with minor circumstantial evidence aspects.

The Court of Appeals was clearly correct in holding (Pet. App. 11) that the specific omissions alone were sufficient to support the verdict. The infirmities of the collateral circumstantial proof are insufficient to vitiate that verdict. *United States* v. *Burdick,* 221 F. 2d 932 (C. A. 3), certiorari denied, 350 U. S. 831; *Cf. Goldbaum* v. *United States,* 222 F. 2d 360 (C. A. 9), certiorari dismissed, 350 U. S. 801; *Beaty* v. *United States,* 220 F. 2d 681 (C. A. 4), certiorari denied, 349 U. S. 946.

2. Petitioner suggests (Pet. 22–23) that since his wife, in his absence, signed his name to the return in question without express authorization from him, it is not really a return. The information alleged that petitioner wilfully attempted to evade a large part of his 1947 income taxes by "filing and causing to be filed * * * a false and fraudulent income tax return" (R. 1). It is clear that petitioner caused the document to be filed, for in keeping with his usual custom he left its preparation to his accountant from the figures in the so-called Cash Book (R. 152, 167). The fact that the wife did sign petitioner's name (R. 141, 167) and that the document was not repudiated by him during the six years inter-

vening between the filing and the trial is some evidence that she was authorized to sign (At the trial he did not deny that she had authority to sign, but testified that he had not discussed the matter with her and believed that she "assumed" she had the right to sign it (Supp. R. 6)). This question was not raised at the trial, and the court charged the jury as follows (R. 199):

> It appears that Mrs. Canton signed the 1947 income tax return. She signed her husband's name. It is not contended that she did not have authority from defendant to sign this return, so it is conceded that the return, Government's Exhibit 1, constitutes defendant's income tax return regardless of the fact that he did not sign it. However, the fact that he was not present when the income tax return was prepared by Mr. Holl, and that he was not present when his wife signed it, is a matter that you may give due consideration to insofar as it may bear upon the question of his alleged intent to wilfully and intentionally commit the offense charged in this information.

Petitioner made no objection to this instruction and is in no position to pursue the point here. *Johnson* v. *United States,* 318 U. S. 189, 199–201, rehearing denied, 318 U. S. 801; Rule 30, Federal Rules of Criminal Procedure. In any event, the error, if any, was highly technical and was in no way prejudicial to petitioner, for the informa-

tion sufficiently informed him of the crime charged so that he could adequately prepare his defense and could plead the judgment in bar of another trial for the same offense. *Gariepy* v. *United States,* 220 F. 2d 252, 259 (C. A. 6), certiorari denied, 350 U. S. 825; cf. *United States* v. *Albanese,* 224 F. 2d 879, 881 (C. A. 2), certiorari denied, 350 U. S. 845.

CONCLUSION

The decision of the court below is clearly correct, and no question warranting review is presented. The petition for a writ of certiorari should be denied.

Respectfully submitted.

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